92-1802

No. 92-

Supreme Court, U.S.
FILED
APR 16 1993
OFFICE OF THE CLERK

IN THE
SUPREME COURT OF THE UNITED STATES

October Term, 1992

VERSYSS INCORPORATED,

Petitioner,

v.

COOPERS & LYBRAND, A PARTNERSHIP;
WILLIAM K. O'BRIEN,
AS MANAGING PARTNER OF COOPERS & LYBRAND,

Respondents.

ON PETITION FOR WRIT OF CERTIORARI TO THE
UNITED STATES COURT OF APPEALS FOR THE FIRST CIRCUIT

PETITION FOR WRIT OF CERTIORARI

PATRICK J. SHARKEY
Counsel of Record,
HENRY A. SULLIVAN
JOHN F. SYLVIA
MINTZ, LEVIN, COHN, FERRIS,
GLOVSKY AND POPEO, P.C.
One Financial Center
Boston, Massachusetts 02111
(617) 542-6000
Counsel for Petitioner

April 19, 1993

QUESTION PRESENTED

1. Whether state corporate and merger law, and the degree of investment experience and business sophistication of a corporate investor, are relevant factors in determining whether the remedial liability provisions of Section 11 of the Securities Act of 1933 apply to a corporate merger premised on an exchange of securities, including publicly traded securities issued pursuant to a Section 11 Registration Statement less than one year prior to the merger?

LIST OF PARTIES

The parties to this proceeding are listed in the caption. Pursuant to Rule 29.1 of this Court, petitioner states as follows: VERSYSS Incorporated; VERSYSS has no parent company, and no subsidiary company required to be disclosed by Rule 29.1.

TABLE OF CONTENTS

QUESTION PRESENTED i

LIST OF PARTIES ii

OPINIONS BELOW 1

JURISDICTION 1

STATUTORY PROVISIONS INVOLVED 1

STATEMENT OF THE CASE 2
- A. Introduction 2
- B. The NDS Merger 3
- C. The District Court Decision 6
- D. The Decision of the Court of Appeals 7

REASONS FOR GRANTING THE WRIT 10
- I. THE MAJORITY OPINION OF THE COURT OF APPEALS MARKS A RADICAL DEPARTURE FROM THE BROAD REMEDIAL PURPOSE OF FEDERAL SECURITIES LAWS WHICH AFFORD PROTECTION TO ALL INVESTORS ACQUIRING SECURITIES 10
  - A. *Section 11 Of The 1933 Act Is A Broad Remedial Liability Provision Designed To Protect All Investors, Including Experienced Corporate Investors.* 11
  - B. *The First Circuit Panel's Split Decision Adopts An Unwarranted And Narrow Interpretation Of Section 11 Which Departs From The Liberal Construction Of Federal Securities Law, Including Application of Section 10(b) Of The Securities Exchange Act Of 1934 In The Context Of A Merger.* 12

II. THE MAJORITY OPINION OF THE COURT OF APPEALS IMPROPERLY PREDICATES APPLICABILITY OF THE 1933 ACT UPON STATE CORPORATION AND MERGER LAW AND THE BUSINESS EXPERIENCE OF THE PARTICULAR PLAINTIFF BEFORE THE COURT 15

CONCLUSION 17

TABLE OF AUTHORITIES CITED

CASES.

Andrews v. *Blue*, 489 F.2d 367 (10th Cir. 1973) 16

Dasho v. *Susquehanna Corp.*,
380 F.2d 262 (7th Cir. 1967) 15

Ernst & Ernst v. *Hochfelder*, 425 U.S. 185 (1976) 11, 12

Herman & MacLean v. *Huddleston*,
459 U.S. 375, 381-82 (1983) 10, 12

In re Penn Central Securities Litigation,
494 F.2d 528 (3d Cir. 1974) 13, 14

Junker v. *Crory*,
650 F.2d 1349 (5th Cir. 1981) 13

Landreth Timber Co. v. *Landreth*, 471 U.S. 681 (1985) 9

Mader v. *Armel*, 402 F.2d 158 (6th Cir. 1968) 15

SEC v. *Capital Gains Research Bureau*,
375 U.S. 180 (1963) 11

SEC v. *National Securities, Inc.*,
393 U.S. 453 (1969) 12-14, 16

SEC v. *Ralston Purina Co.*, 346 U.S. 119 (1953) 11

SEC v. *W.J. Howey Co.*, 328 U.S. 293 (1946) 11

Smallwood v. *Pearl Brewing Co.*,
489 F.2d 579 (5th Cir. 1974) 15

Vine v. *Beneficial Finance Company*, 374 F.2d 627 (2d Cir.) 15

Woolf v. *S.D. Cohn & Company*, 515 F.2d 591 (5th Cir. 1975) 9

Young v. *Mader*, 394 U.S. 930 (1969) 15

STATUTES AND RULES.

15 U.S.C. § 77d(2) 9

15 U.S.C. § 77k(a) *passim*

15 U.S.C. § 77k(b) 7

15 U.S.C. § 77k(e) *passim*

15 U.S.C. § 78j(b) 12

28 U.S.C. § 1254(1) 1

OTHER.

5C Arnold S. Jacobs, SECURITIES LAW SERIES, LITIGATION AND PRACTICE UNDER RULE 10B-5, § 117.02, p. 5-76 (Clark Boardman Co. Ltd., 2d Ed. 1991) 13

H.R. Rep. No. 85, 73rd Cong., 1st Sess., 1-5 (1933)) 10

Petitioner VERSYSS Incorporated ("VERSYSS") respectfully prays that a Writ of Certiorari issue to review the Judgment and Opinion of the United States Court of Appeals for the First Circuit entered on December 30, 1992.

OPINIONS BELOW

The decision of the United States Court of Appeals for the First Circuit affirming the grant of summary judgment by the United States District Court for the District of Massachusetts in favor of Respondents Coopers & Lybrand and its Managing Partner William K. O'Brien (collectively "C&L") is reported at 982 F.2d 653, and is reprinted starting at page A1.[1] The District Court decision from which the appeal was taken is dated January 15, 1992 and is reprinted starting at page A16.

JURISDICTION

Judgment on the decision of the Court of Appeals was entered on December 30, 1992. Petitioner timely sought rehearing pursuant to Fed. R. App. P. 35. On January 21, 1993, the United States Court of Appeals for the First Circuit denied rehearing. The order denying the petition for rehearing is reprinted at A15. The jurisdiction of this Court is invoked pursuant to 28 U.S.C. § 1254(1).

STATUTORY PROVISIONS INVOLVED

The question presented involves the interpretation and application of Section 11 of the Securities Act of 1933, as codified in Title 15 of the United States Code, in the context of a merger. The specific provisions involved are:

15 U.S.C. § 77k(a)
15 U.S.C. § 77k(b)
15 U.S.C. § 77k(e)

These provisions are reprinted in the Appendix at A26 *et seq.*

---

[1]References to "A__" are to the Appendix to this Petition.

STATEMENT OF THE CASE

A. Introduction.

The 1980s witnessed a watershed realignment of corporate culture evidenced by an unprecedented number of recapitalizations, corporate takeovers and mergers. These transactions were fueled by creative entrepreneurs and financial wizards packaging and marketing a myriad of securities offerings, often facilitated by expert reports included in Registration Statements for initial public offerings. Regrettably, the 1980s also ushered in an era of unparalleled securities law abuse, often aided by accountants and other professionals lending their touted expertise to support capital formation through those initial public offerings. Until now, the uniform judicial response to such excesses in transactions involving securities has been guided by a flexible and practical application of the federal securities laws to effectuate a broad remedial purpose -- disclosure of accurate and complete information for the protection of all persons acquiring securities, including so-called "sophisticated" corporate investors. All that has been changed, however, by the decision of the United States Court of Appeals for the First Circuit which is the subject of this Petition.

Eschewing the breadth accorded the federal securities laws by this Court and other appellate courts requiring accurate disclosure in the context of securities transactions, in a 2-1 decision the First Circuit adopted an interpretation of Section 11 of the 1933 Act ("1933 Act") conditioning imposition of liability for false Registration Statements on the form of corporate merger vehicle, without due regard for the substance of the transaction, while also making the business sophistication of the plaintiff and

the plaintiff's corporate status important considerations.[2] That approach, however, makes application of Section 11 to any particular merger random and arbitrary because, in the view of the First Circuit, whether federal law applies is dependent upon the particulars of governing state corporate and merger law and the particular characteristics of the parties to the transaction. This new approach by the majority First Circuit opinion to application of the 1933 Act, which was flatly rejected in a strong dissenting opinion, eliminates the flexible remedial character of the securities laws by elevating form over substance and ignores the need of all parties to a transaction to receive disclosure so that the available level of sophistication of the parties, whatever that may be, can be applied in an environment of accurate and complete information. Because the world of finance only promises to become more creative and complex, any attempt to scale back the protection afforded to all investors should be scrutinized by this Court before achieving any currency in the universe of merger and acquisition precedent.

B. The NDS Merger.

On or about May 17, 1985, (i) Northern Data Systems, Inc. ("NDS"), the (ii) founding shareholders of NDS, (iii) Contel Corporation ("Contel"), and (iv) Contel's wholly-owned subsidiary, NDS Merger Corporation, entered into a Merger Agreement entitled "Continental Telecom Inc., NDS Merger Corporation, Northern Data Systems Inc. and Certain Founding Stockholders' Agreement and Plan of Reorganization" (the

---

[2]Section 11(a) provides, in relevant part:

> In case any part of the registration statement, when such part became effective, contained an untrue statement of a material fact or omitted to state a material fact required to be stated therein or necessary to make the statements therein not misleading, any person acquiring such security ... may ... sue ... every accountant ... with respect to the statement in such registration statement, report, or valuation which purports to have been prepared or certified by him ....

"Merger Agreement"). JA-143-75.[3] As of the Merger Agreement and the effective date of the Merger, the outstanding capital stock of NDS included publicly-held stock issued and sold less than one year earlier, in August, 1984, pursuant to a Prospectus and Registration Statement (the "Registration Statement") in connection with an initial public offering by NDS. That Registration Statement included financial statements audited by Respondent C&L and unqualified expert audit reports by C&L on those financial statements. JA-96. Contel alleges that it relied on the C&L audit reports in acquiring NDS securities in the 1985 Merger.

In substance, the Merger Agreement provided for NDS to be merged with and into NDS Merger Corporation, a single-purpose, wholly-owned subsidiary of Contel, after satisfaction of enumerated conditions precedent (the "Merger"). As contemplated by the parties in this triangular "forward" merger (a merger vehicle commonly used in the corporate world in which NDS, the acquired corporation, disappeared upon consummation of the Merger), Contel and NDS published a Combined Proxy Statement-Prospectus dated June 14, 1985 (the "Prospectus") for the purpose of soliciting approval of the Merger by NDS stockholders. JA-179-226. The Prospectus outlined, *inter alia*, the relevant matters attendant to the issuance and deliverance of Contel common stock to NDS stockholders in exchange for NDS common stock in connection with the Merger. JA-181-82.

The Merger Agreement was approved at a special NDS stockholders' meeting held on July 16, 1985, two months after execution of the Merger Agreement. The "Closing" of the Merger, referred to in Section 3 of the Merger Agreement, was held on that same day after the stockholders' meeting. JA-132, 149 and 193. Contel, the sole stockholder of NDS Merger Corporation, approved the proposed Merger Agreement prior to

---

[3]References to JA-__ are to the Joint Appendix filed with the appeal to the United States Court of Appeals for the First Circuit.

July 16, 1985. All conditions precedent to the Merger set forth in Sections 11 and 12 of the Merger Agreement, including preparation and delivery of documents contemplated by the Merger Agreement, were satisfied at or before the Closing. JA-193.

The Prospectus detailed the mechanics under state law involved in Contel's acquisition of the NDS stock in connection with the Merger as follows:

> Upon consummation of the Merger, each issued and outstanding share of the common stock, $1.00 par value per share, of NDS ("NDS Stock") will be converted into shares of the common stock, $1.00 par value per share, of Contel ("Contel Stock") ***in the manner described below in this Proxy Statement-Prospectus***.

JA-179 (emphasis added). With respect to the manner of the bargained-for exchange and automatic conversion of NDS securities in exchange for Contel securities the Prospectus stated:

> At the Special Meeting, the holders of NDS Stock will consider and vote upon a proposal to approve the Merger Agreement (. . .), providing for the merger of NDS with and into Contel Subsidiary, ***and for the exchange of all outstanding shares of NDS Stock for shares of Contel Stock*** pursuant to a formula under which each share of NDS Stock will be valued at $11.00.

JA-184 (emphasis added).

The exchange of securities at the core of the Merger is the heart of the Merger Agreement:

> . . . each share of NDS Stock issued and outstanding on the Effective Date (other than

> treasury shares) shall, as of the Effective Date, by virtue of the Merger and without any action on the part of the holder thereof, ***be converted into and exchanged for*** the number of shares of Contel Stock determined by dividing $11.00 by the Valuation Price.

JA-148 [Merger Agreement, § 2.2(a)] (emphasis added). In addition, the Merger Agreement provided for payment, pursuant to the Massachusetts Business Corporation Law, of the value of the NDS shares held by any stockholder dissenting to the Merger. JA-150.

In short, the Prospectus and Merger Agreement highlighted and detailed the mechanics of state corporate and merger law, in this particular instance Delaware and Massachusetts law, by which Contel was to acquire all outstanding NDS securities in a bargained-for exchange of securities. The Merger Agreement contemplated: (i) satisfaction of all conditions precedent at or before a closing on the Merger, including shareholder votes and delivery of certain documents; (ii) the filing of documents with the Secretaries of State of Delaware and Massachusetts making the Merger effective; (iii) the exchange of NDS common stock securities for Contel stock upon the effective time of the Merger; (iv) the acquisition by Contel of NDS stock certificates in exchange for Contel stock; and (v) payment for NDS common stock securities to dissenting NDS stockholders in exchange for surrender of NDS stock certificates. JA-147-68.

C. The District Court Decision.

On January 15, 1992, the District Court issued entry of a Final Judgment granting C&L summary judgment on the VERSYSS Section 11 claim (the only VERSYSS claim arising under federal law in this non-diversity case). The District Court also dismissed, without prejudice, pendent state law claims.

A25.[4] Focusing on the language of Section 11, particularly the phrase "acquiring such security (A14, emphasis added)," the District Court reasoned that as a result of the Merger Agreement and the merger process (at least as a matter of state corporate law governing this particular merger), the NDS securities acquired by Contel were not the same securities as those issued pursuant to the Registration Statement. Thus, without defining exactly what was acquired in the Merger, the District Court concluded that Contel did not acquire, and "never received or had a right to receive securities ***having the same characteristics*** as those issued pursuant to the allegedly erroneous prospectus and registration statement (emphasis added)." A20.[5]

D. The Decision of the Court of Appeals.

While noting that Section 11 was "now brought to bear on a transaction that Congress probably did not consider," the Court of Appeals, by a 2 to 1 margin, affirmed the District Court. A2. Although the divided Court of Appeals recognized that the

---

[4]Those state law claims, which the District Court and the Court of Appeals both pointed to as a putative source of comfort for VERSYSS notwithstanding dismissal of the Section 11 claim, require VERSYSS to carry the burden of proof that C&L was negligent. In sharp contrast, however, Section 11(b) of the 1933 Act places the burden on C&L to prove that it was not negligent:

> "no person, other than the issuer, shall be liable as provided therein who shall sustain the burden of proof -- . . . [that] he had, after reasonable investigation, reasonable ground to believe, at the time such part of the registration statement became effective, that the statements therein were true and that there was no omission to state a material fact required to be stated therein or necessary to make the statements therein not misleading. . . ."

In a complex accountant liability trial before a jury, allocation of the burden of proof often is outcome determinative.

[5]There is no issue concerning the "tracing" of NDS securities acquired by Contel in 1985 back to the 1984 Registration Statement involved in this Section 11 case. All securities issued by NDS, including those issued pursuant to the Registration Statement were acquired by Contel in the Merger.

definition of "security" traditionally has been given a broad construction by all federal courts, including this Court, the majority applied Delaware corporate law principles as the linchpin for holding that the Merger Agreement and the Merger effectuated a transformation of the character of NDS securities, thereby making what Contel acquired in the Merger something other than securities; however, like the District Court, the Court of Appeals never quite defined what Contel did acquire in the Merger.[6]

The Court of Appeals concluded its analysis with an examination of the history of events spawning the enactment of the federal securities laws. A6-9. Although the majority opinion recognized that "the broad purpose of the 1933 Act was to require full disclosure to investors," it questioned, pointedly, whether Congress intended the securities laws to protect corporate merger investors as opposed to "ill-informed small investors". A7. The clear and unequivocal pronouncement that federal securities laws do not offer protection to sophisticated

---

[6]Thus, the First Circuit majority opinion did not agree with the District Court's rationale. The District Court concluded that Contel acquired securities in the Merger which, as a result of the application of state corporate and merger law, were different in character from the NDS securities issued pursuant to the Registration Statement. The Court of Appeals, on the other hand, found that no securities were acquired by Contel in the Merger. *Compare* A6 with A20.

The Court of Appeals also focused on the Section 11 damage formula as a "second piece of evidence" suggesting that VERSYSS did not have a Section 11 claim. A7-8. Applying a literal reading of the statutory formula, the Court of Appeals concluded that "the continuation of the acquired securities in the hands of the plaintiff-buyer is a premise of the damage calculation." A7. The Court of Appeals conceded, however, that the damages formula was workable even where the form of the transaction presented obstacles to the application of the statute. Indeed, as the Court of Appeals majority opinion even recognized, had Contel acquired the NDS securities in a tender offer and then merged NDS into the Contel Subsidiary, Section 11 arguably would apply. ("Doubtless some formula could be jury-rigged to replicate the substance of section 11(e), were the merger to be treated as an acquisition of NDS Securities by Contel"). A8. Yet, the application of the damages formula in that instance would be no more difficult than in the context of the Merger.

corporate investors marks a wholesale departure from well-established precedent of this Court.[7]

In a strong and cogent dissent, Judge Torruella challenged the majority's formalistic application of Section 11, urging that the proper inquiry requires focus on the substance of the Merger and the application of the plain language of Section 11. ("I arrive at my conclusion by reading the plain language of § 11 and deferring to the ordinary and common meaning of its words"). A13. As framed by the dissent, the dispositive issue was "whether VERSYSS ever gained possession, control or power of disposal over NDS stock." A13. Judge Torruella then disposed of the issue by concluding that "Contel gained its ability to extinguish NDS stock as a result of its acquisition." A13.

Furthermore, unlike the majority, which saw no reason to include "sophisticated" corporate investors under the umbrella of Section 11 protection, the dissent recognized that Section 11 is to be construed "'flexibly to effectuate its remedial purpose'" and then reasoned that interpreting Section 11 to apply to the particular type of merger at issue furthered Congress' goal of controlling unsound and fraudulent business practices. A14. In sharp contrast, by unnecessarily restricting the reach of the 1933 Act the majority's holding undercuts that broad remedial purpose of Section 11.

---

[7]For example, in contrast to the First Circuit's statements about sophisticated corporate investors not needing or being entitled to the protection of the securities laws, this Court has held that even those securities transactions exempt from registration requirements, such as private placements involving so-called "sophisticated investors", remain subject to the antifraud provisions of federal securities laws, including the 1933 Act. *Landreth Timber Co.* v. *Landreth*, 471 U.S. 681, 692 (1985) ("although § 4(2) of the 1933 Act, 15 U.S.C. § 77d(2) [], exempts transactions not involving any public offering from the Act's registration provisions, there is no comparable exemption from the antifraud provisions). *See also Woolf* v. *S.D. Cohn & Company*, 515 F.2d 591, 607 (5th Cir. 1975) (while securities may be exempt from the registration requirements of the 1933 Act, the same high duty which is owed to prospective investors in public offerings remains).

REASONS FOR GRANTING THE WRIT

I. THE MAJORITY OPINION OF THE COURT OF APPEALS MARKS A RADICAL DEPARTURE FROM THE BROAD REMEDIAL PURPOSE OF FEDERAL SECURITIES LAWS WHICH AFFORD PROTECTION TO ALL INVESTORS ACQUIRING SECURITIES

By holding that the mechanics and method of acquisition, and consequences flowing therefrom under state law, determine whether federal securities law applies to transactions in which securities are exchanged, and by suggesting that the investment experience and corporate status of the plaintiff also merit strong consideration, the Court of Appeals has set a dangerous precedent by exalting form over substance and leaving so-called "sophisticated" corporate investors stripped of protection under federal securities law. Neither the plain language of the 1933 Act nor the Congressional intent behind it provides for elimination of Section 11 protections in these circumstances. Given the multitude of mergers which will continue to be consummated among sophisticated corporate parties, placing unnecessary limitations on exacting federal disclosure standards for investors of all levels of experience threatens a revival of the same sharp practices the federal securities laws were promulgated to correct. Accordingly, this Court should review the Court of Appeals' Decision and correct an unwarranted deviation from the fundamental purpose underlying Section 11 of the 1933 Act.[8]

---

[8] *Herman & MacLean* v. *Huddleston*, 459 U.S. 375, 381-82 (1983) ("[Section 11] was designed to assure compliance with the disclosure provisions of the [1933] Act by imposing a stringent standard of liability on the parties who play a direct role in a registered offering").

A. *Section 11 Of The 1933 Act Is A Broad Remedial Liability Provision Designed To Protect All Investors, Including Experienced Corporate Investors.*

The securities laws were not intended to be construed "technically and restrictively, but flexibly [in order] to effectuate [their] broad remedial purposes."[9] As emphasized by this Court:

> [t]he Securities Act of 1933 . . . was designed to provide investors with full disclosure of material information concerning public offerings of securities in commerce, to protect investors against fraud and, through the imposition of specified civil liabilities, to promote ethical standards of honesty and fair dealing.[10]

The formalistic approach embraced by the majority opinion undercuts this broad remedial mandate. Indeed, the Decision patently ignores this Court's long-standing admonition that the ***economic realities*** of the transaction govern the applicability of federal securities law.[11] Here, the economic realities could not be more plain: Contel elected to acquire NDS securities for a price determined, in part, in reliance on representations by C&L in audit reports included, with the consent of C&L, in a Registration Statement. To subvert the economic realities of the transaction to the vagaries of each state's corporate and merger law and the sophistication level of each particular plaintiff deviates from the language as well as the underlying purpose of Section 11, a remedial statute which draws no such distinctions.

---

[9] *SEC v. Capital Gains Research Bureau*, 375 U.S. 180 (1963).

[10] *Ernst & Ernst* v. *Hochfelder*, 425 U.S. 185, 195 (1976) (*citing* H.R. Rep. No. 85, 73rd Cong., 1st Sess., 1-5 (1933)). *See also SEC* v. *Ralston Purina Co.*, 346 U.S. 119, 124 (1953) (purpose of the 1933 Act is to protect the investor by promoting full disclosure of information considered necessary to make informed investment decisions).

[11] *SEC* v. *W.J. Howey Co.*, 328 U.S. 293, 298-301 (1946).

Moreover, the Decision sets a precedent which encourages the growth of transactions designed to avoid the curbing influence of Section 11 -- a result which Congress certainly did not intend.[12]

B. *The First Circuit Panel's Split Decision Adopts An Unwarranted And Narrow Interpretation Of Section 11 Which Departs From The Liberal Construction Of Federal Securities Law, Including Application Of Section 10(b) Of The Securities Exchange Act Of 1934 In The Context Of A Merger.*

As this Court has recognized, "the interdependence of the various securities laws is certainly a relevant factor in any interpretation of the language Congress has chosen . . . ."[13] Where, as here, the parameters of Section 11 have yet to be defined with respect to merger transactions, the extensive body of case law developed in the context of Section 10(b) of the Securities Exchange Act of 1934 analyzing the treatment accorded to securities exchanged in a merger warrants close consideration by this Court at this time.

---

[12]The triangular forward merger format, in which the acquired corporation is extinguished (as NDS was extinguished in the Merger), is generally prompted by favorable tax consequences. In substance, however, a forward triangular merger is no different than a reverse triangular merger in which the acquired corporation survives (in which case Contel's subsidiary, NDS Merger Corporation, would have been merged with and into NDS as the surviving corporation). Both the District Court (A22-23) and the Court of Appeals (A8 and A10) appear to concede that if the form and direction of the Merger had been reverse triangular instead of forward triangular, a Section 11 claim would exist. Since the substance of the Merger remains unchanged by the precise form used -- whether forward or reverse -- the Decision is the penultimate elevation of form over substance.

[13]*SEC* v. *National Securities, Inc.*, 393 U.S. 453, 466 (1969). *See also Ernst & Ernst* v. *Hochfelder*, 425 U.S. 185, 206 (the 1933 Act and 1934 Act "constitute interrelated components of the federal regulatory scheme governing transactions in securities"); *Herman & MacLean* v. *Huddleston*, 459 U.S. 375 at 386 (1983)("[a] cumulative construction of the securities laws also furthers their broad remedial purposes").

In substance, Section 10(b) imposes liability on any person who employs any manipulative or deceptive device in connection with the "purchase or sale" of securities.[14] Not surprisingly, defendants routinely have urged a restrictive reading of the "purchase or sale" requirement in attempts to escape Section 10(b) liability for fraudulent acts committed in the course of merger transactions, but this approach has been soundly rejected. In this regard, the Third Circuit summarized the law as follows while being guided closely by this Court:

> It is well established that the share exchange accompanying the merger of two separate and distinct corporate entities, pursuant to which shareholders of one or both of the original entities exchange their shares for shares in the surviving or newly created corporation constitutes a purchase or sale bringing the transaction within the scope of 10(b).[15]

Indeed, the rationale underlying the conclusion reached in *National Securities* and *Penn Central* harkens back to the economic realities test. There simply is no substantive difference

---

[14]15 U.S.C. § 78j(b) provides:

> It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce or of the mails, or of any facility of any national securities exchange-
>
> (b) To use or employ, in connection with the purchase or sale of any security registered on a national securities exchange or any security not so registered, any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors.

[15]*In re Penn Central Securities Litigation*, 494 F.2d 528, 533 (3d Cir. 1974) *citing SEC* v. *National Securities, Inc.*, 393 U.S. 453, 464-67 (1969). *See also Junker* v. *Crory*, 650 F.2d 1349, 1359 (5th Cir. 1981) (merger can amount to a purchase or sale of a security for purposes of the 1933 Act).

between an acquisition of stock by merger and a purchase of stock for cash:

> In such a merger between two corporations, the original shareholders of each corporation end up with stock in a substantially different company with substantially different assets and prospects. The decision to vote in favor of the merger is therefore little different from the decision to sell shares in the original corporation and, with the cash received for those shares, buy shares in the merged corporation. ***It clearly effectuates the remedial purposes of the securities acts, therefore, to extend their protections to such a share exchange*** *(emphasis added).*[16]

As succinctly expressed by one leading commentator:

> A merger should be considered from the point of view of the four parties affected by the transaction: the two constituent corporations and their respective stockholders. The corporation surviving a merger sells its securities, which are issued in the merger to stockholders of the disappearing entity, ***and buys their shares***. Stockholders of the disappearing entity therefore buy securities of the surviving corporation and

---

[16] *In re Penn Central Securities Litigation*, 494 F.2d 528, 534 (3d Cir. 1974). While *Penn Central* involved a share exchange where the shares of both pre-merger corporations survived the merger, the rationale is equally applicable where the exchanged shares of one corporation are extinguished pursuant to the merger. Indeed, the *Penn Central* opinion, 494 F.2d at 533, expressly relied on *SEC* v. *National Securities* -- a case in which the exchanged shares of the acquired corporation were extinguished -- as support for its analysis.

> sell their stock in the disappearing company (emphasis added).[17]

This "purchase or sale" analogy should be applied to the interpretation and application of Section 11 in the merger context. Where the target corporation's shareholders in a merger ***exchange*** their securities for securities of an acquiring corporation, the fact that target corporation's shares are extinguished in connection with that same exchange as a matter state merger jurisprudence should be irrelevant. To hold otherwise creates an artificial distinction promoting random and arbitrary results not warranted by existing case law and at odds with the legislative purpose underlying promulgation of the federal securities laws. *See* n.12, *supra*.

II. THE MAJORITY OPINION OF THE COURT OF APPEALS IMPROPERLY PREDICATES APPLICABILITY OF THE 1933 ACT UPON STATE CORPORATION AND MERGER LAW AND THE BUSINESS EXPERIENCE OF THE PARTICULAR PLAINTIFF BEFORE THE COURT

The Decision rests upon the premise that Delaware corporate merger law provides that the NDS stock underwent a considerable transformation when the Merger became effective.

---

[17] 5C Arnold S. Jacobs, *5C Arnold S. Jacobs, SECURITIES LAW SERIES, LITIGATION AND PRACTICE UNDER RULE 10B-5*, § 117.02, p. 5-76 (Clark Boardman Co. Ltd., 2d Ed. 1991). *See also Mader* v. *Armel*, 402 F.2d 158, 160-61 (6th Cir. 1968) (the exchange of stock in the merger of two separate corporations constitutes a sale within the meaning of the 1934 Act), *cert. denied sub nom. Young* v. *Mader*, 394 U.S. 930 (1969); *Dasho* v. *Susquehanna Corp.*, 380 F.2d 262, 266 (7th Cir. 1967) ("... there is no inherent distinction under the Securities and Exchange acts between a corporate sale of stock for cash and the relative impact on the corporate shares of two corporations resulting from their merger"); *Vine* v. *Beneficial Finance Company*, 374 F.2d 627, 635 (2d Cir.), *cert. denied*, 389 U.S. 970 (1967) (short form merger which results in exchange of stock constitutes a purchase and sale under Section 10(b) of the 1934 Act); *Smallwood* v. *Pearl Brewing Co.*, 489 F.2d 579, 591 (5th Cir. 1974) (the exchange and conversion of a target corporation's stock in furtherance of a merger transaction constitutes a purchase and sale under Section 10(b) of the 1934 Act).

The fallacy inherent in an approach relying on state law and not federal law is that state corporate law is designed to promote certainty and predictability in corporate transactions. In sharp contrast, federal securities laws, including Section 11, are designed to protect investors in a wide-range of contexts involving securities regardless of the form of transaction. To make the applicability of federal law designed to evolve and meet challenges posed by new forms of securities transactions contingent upon stagnant state law concepts invites a departure from a uniform application of the securities laws in favor of disparate and random application of federal law dependent upon the particular state law applied and the characteristics of the particular plaintiff before the court.

Notably, the federal courts have had little difficulty fashioning federal securities law remedies irrespective of the transactional permutations cognizant under state law.[18] The Decision, however, abandoned the broad remedial protections of the federal securities laws in favor of corporate formalism and an unwarranted focus on the business experience and character of the plaintiff. *See* nn. 12 and 7, *supra*. As this result promises to create an uneven and, indeed, arbitrary application of the federal securities laws dependent upon which state corporate and merger law applies, and the investment experience and business sophistication of each particular plaintiff, Petitioner submits that the Decision merits review by this Court for these important reasons.

---

[18] *See, e.g., SEC* v. *National Securities, Inc.*, 393 U.S. 453, 467 (1969) ("[w]hatever the terms 'purchase' and 'sale' may mean in other contexts, here an alleged deception has affected individual shareholders' decisions in a way not at all unlike that involved in a typical cash sale or share exchange."); *Andrews* v. *Blue*, 489 F.2d 367, 376 and n.8 (10th Cir. 1973) (exchange of ownership interest in a merger is a 'purchase or sale' under Rule 10b-5).

CONCLUSION

For the foregoing reasons, Petitioner urges this Court to grant the Petition for a Writ of Certiorari to review the decision of the United States Court of Appeals for the First Circuit in this matter.

Respectfully submitted,

VERSYSS Incorporated

PATRICK J. SHARKEY
Counsel of Record,
HENRY A. SULLIVAN
JOHN F. SYLVIA
MINTZ, LEVIN, COHN, FERRIS,
GLOVSKY AND POPEO, P.C.
One Financial Center
Boston, Massachusetts 02111
(617) 542-6000
Counsel for Petitioner

April 19, 1993

Table of Contents.

Appendix A
Decision of the United States Court of Appeals for the First Circuit dated December 30, 1992 A1

Appendix B
Denial of Petition for Rehearing dated January 21, 1993 A15

Appendix C
Decision of the United States District Court for the District of Massachusetts dated January 15, 1992; Final Judgment dated January 15, 1992 A16

Appendix D
Statutes A26

Appendix A.

UNITED STATES COURT OF APPEALS

FOR THE FIRST CIRCUIT

(Argued: July 31, 1992 Decided: December 30, 1992
Docket No. 92-1212

VERSYSS INCORPORATED,

Plaintiff-Appellant,

—v.—

COOPERS & LYBRAND, A PARTNERSHIP
AND WILLIAM K. O'BRIEN, AS MANAGING PARTNER OF
COOPERS & LYBRAND,

Defendants-Appellees.

Before:

Torruella, Cyr and Boudin,

Circuit Judges.

[PATRICK J. SHARKEY] (Henry A. Sullivan, John F. Sylvia, and Mintz, Levin, Cohn, Ferris, Glovsky, and Popeo, P.C., Boston, MA of counsel) [*for plaintiff, appellant*]

[STEVEN W. PHILLIPS] (Christian M. Hoffman, Peter M. Casey and Foley, Hoag & Eliot, Boston, MA of counsel) [*for defendants, appellees*].

BOUDIN, [*Circuit Judge*]:

This case presents a common problem in statutory interpretation. Congress drafted a law that clearly embraces some transactions, clearly excludes others, and is now brought to bear on a transaction that Congress probably did not consider. We are left to make a judgment based on clues garnered from statutory language, legislative history, purpose and policy. In our view, the transaction at issue does not fit comfortably within the statutory language, and no clear policy or precedent encourages courts to extend that language beyond its normal bounds.

I.

On May 17, 1985, Continental Telecom, Inc. ("Contel") entered into a merger agreement with Northern Data Systems, Inc. ("NDS"). The agreement provided that NDS would be merged into a newly created subsidiary of Contel and, in exchange, NDS stockholders would receive Contel stock. Both Contel and its merger subsidiary were Delaware corporations; NDS was a Massachusetts corporation. At the time of the merger agreement, NDS stock was publicly traded. Previously, a registration statement under the Securities Act of 1933 had been filed with the Securities and Exchange Commission in connection with an August 1984 public offering of NDS stock. See sections 5-16, 15 U.S.C. §§ 77e-77p.

The merger was approved by NDS stockholders, and NDS was merged into the Contel subsidiary on July 16, 1985. In accordance with the merger agreement, Contel's subsidiary, as the surviving corporation, acquired effective ownership of the assets, and responsibility for the debts, of the former NDS. The merger agreement provided that on the date of the merger, the "separate corporate existence of NDS shall terminate." Thereafter, in accordance with the merger agreement, the former NDS stockholders sent in their now defunct NDS stock certificates to Contel's exchange agent and received their Contel stock certificates.

Subsequent to the merger, Contel concluded that the NDS registration statement had contained materially misleading financial information, including information certified by the accounting firm of Coopers & Lybrand. Although the registration statement had been issued before the merger, section 11 of the Securities Act of 1933, 15 U.S.C. § 77k, imposes (subject to certain limitations) continuing liability for misstatements or material omissions in registration

statements; after the registration statement becomes effective, a federal damage action may be brought, by "any person acquiring such security," against any of a list of specific responsible persons, including the certifying accounting firm. Section 11(a), 15 U.S.C. § 77k(a). Accordingly, the present suit, now conducted by Versyss Incorporated as Contel's assignee, was brought against the accounting firm of Coopers & Lybrand.

In the district court, Coopers & Lybrand moved for summary judgment on the ground that Contel did not qualify as a section 11 plaintiff because it had not "acquired [NDS] securit[ies]." Patently, Contel "acquired" *something* in exchange for the many Contel shares it issued in the merger, so the focus of the dispute is upon the term "security." Pointing to the transfer of the NDS certificates, Versyss claimed that NDS securities were acquired by Contel through the merger. The district court, adopting Cooper & Lybrand's view of the matter, held that the NDS stock certificates were an empty shell not qualifying as a "security" and that the essence of what Contel received was the assets and liabilities of the former NDS. The district court then granted summary judgment for Coopers & Lybrand on the section 11 claim, dismissing pendant state claims without prejudice. This appeal followed.

II.

Statutory construction begins with statutory language. The language in this case is straightforward: section 11 of the Securities Act of 1933, so far as pertinent here, creates a federal cause of action in favor of a purchaser "acquiring a security" after a false or misleading registration statement for that security has gone into effect unless the defendant makes out a statutory defense comprising, in general terms,

reasonable inquiry and good faith belief. Section 11(a)(4), (b), 15 U.S.C. §§ 77k(a)(4), (b).

The term "security" is defined in both the Securities Act of 1933 and Securities Exchange Act of 1934, provisions which despite differences in language are construed alike. *Landreth Timber Co.* v. *Landreth*, 471 U.S. 681, 686 n. 1, 105 S.Ct. 2297, 2301 n. 1, 85 L.Ed.2d 692 (1985). Nothing in the language of the definitions precisely resolves the present issue except so far as the variety and breadth of the definitions encourage a broad construction.[1/] But terms, even broadly construed, have outer limits, and those limits are strained badly by describing what Contel acquired through the merger as a "security."

On the date of the merger, and before any NDS stock certificates were to be transferred to Contel's exchange agent, NDS ceased to exist as a corporation. This is ordinary merger-law jurisprudence *(Frandsen* v. *Jensen-Sundquist Agency, Inc.*, 802 F.2d 941, 944 (7th Cir. 1986) ("in a merger the shares of the acquired firm are not bought, they are extinguished")) and accords with the Contel-NDS agreement already quoted. Delaware's merger

---

[1/] The 1933 Act definition, section 2(1), 15 U.S.C. § 77b(1), provides:

> "The term "security" means any note, stock, treasury stock, bond, debenture, evidence of indebtedness, certificate of interest or participation in any profit-sharing agreement, collateral-trust certificate, preorganization certificate or subscription, transferable share, investment contract, voting-trust certificate, certificate of deposit for a security, fractional undivided interest in oil, gas, or other mineral rights, or, in general, any interest or instrument commonly known as a "security," or any certificate of interest or participation in, temporary or interim certificate for, receipt for, guarantee of, or warrant or right to subscribe to or purchase, any of the foregoing."

statute follows this pattern, providing that in a merger "the separate existence ... of all such constituent corporations except the one into which the other or others ... have been merged ... shall cease.... [and] all property ... shall be vested in the corporation surviving...." Del.Code Ann. tit. 8, § 259(a). *Accord,* Mass. Gen. Laws Ann. ch. 156B, §§ 80(a)(1), (5). Under the same statutes and the merger agreement, upon the merger the assets and liabilities of NDS became those of the surviving Contel subsidiary.

It follows that, when the merger became effective, NDS stock underwent a considerable transformation. At that point, the NDS stock certificates ceased to represent an investment interest in the separate assets of NDS (since it no longer existed), ceased to reflect voting rights in the management of NDS (since NDS ceased to have a management), and ceased to comprise a claim to dividends declared from NDS earnings (since no such dividends could be issued). In sum, for the NDS stock the essential characteristics of securities ceased to pertain. "[A]t the moment a stock for stock merger is effective, the stock in a constituent corporation (other than the surviving corporation) ceases to exist legally." *Shields* v. *Shields*, 498 A.2d 161, 168 (Del. Ch.), *appeal refused,* 497 A.2d 791 (Del. 1985).

If this view is taken, then-when the former NDS stockholders turned in their NDS certificates *after* the merger-what Contel received was not "securities." At worst, the certificates were wall-paper; at best, they represented evidence that the parties who surrendered the certificates were prior owners of NDS stock, entitled by virtue of the merger agreement to be paid the Contel stock promised as consideration. Nor does Contel's position improve if one views the situation at the time after the merger agreement was signed but *before* the merger was consummated. It may be that for some purposes a contract to acquire securities can

be treated as an acquisition. *Cf.* Sections 3(a)(13)-(14) of the 1934 Act, 15 U.S.C. §§ 78c(a)(13)-(14). But, as the trial judge pointed out, the merger agreement in this case between Contel and NDS was not a step on the road to Contel's acquiring of NDS securities but rather was an agreement to merge NDS out of existence.

There is a second piece of evidence, culled from the statutory language, that hinders Versyss' claim. Section 11 provides a damage formula for the cause of action it creates. Simplifying somewhat, Section 11(e) provides that the recovery is to be the difference between the (presumptively higher) price paid for the security when acquired by the plaintiff-buyer and either of three (presumptively lower) numbers: "(1) the value thereof [of the security] as of the time such suit was brought, or (2) the price at which such security shall have been disposed of in the market before suit, or (3) the price at which such security shall have been disposed of after suit but before judgment...." 15 U.S.C. § 77k(e).[2/]

This language assumes a buyer of securities who pays a price for and receives securities. Then, finding that the securities are worth less than the price paid, the buyer brings suit either for the loss of value or, if the buyer sells before suit or before judgment, for the loss suffered on account of the reduced sale price received by the buyer on resale. In sum, the continuation of the acquired securities in the hands of the plaintiff-buyer is a premise of the damage calculation. Yet in this case the NDS securities ceased to exist at the time

---

[2/] Subsection (e) provides a rule for choosing between alternatives (2) and (3) if the security has been disposed of after suit but before judgment, and it has several further limitations and provisos dealing with special circumstances. None of these provisions alters the basic structure of the damage formula.

of merger because the corporation ceased to exist. It would be fantasy to speak of the nonexistent NDS securities as suffering a post-merger decline in value or being resold for less than the purchase price.[3/]

Doubtless some formula could be jury-rigged to replicate the substance of section 11(e), were the merger to be treated as an acquisition of NDS securities by Contel. After all, if Contel acquired all of the NDS securities in a tender offer and then merged the company into its subsidiary, securities would have been "acquired" and an arguable claim would exist under section 11. But the statutory damage provision does limn the transactions toward which Congress directed section 11; and, as we have just seen, the extinction of NDS securities incident to the merger conflicts with section 11's premise of continuity. Viewing the case form the standpoint of damages may itself underscore the nature of Contel's real complaint: that effective upon the merger it acquired *a package of assets and liabilities* formerly pertaining to NDS that was worth less than Contel had been led to believe.

III.

Words normally have some elastic in their makeup. Courts in other cases have stretched language further than Versyss asks us to do in this case. If legislative history or purpose encouraged that result, the question here might be a close one. The difficulty is that an inquiry into history and purpose, if instructive at all, favors the more literal reading of the statute adopted by the district court.

[3/] The section 11 damage remedy was added by amendment in 1934, 48 Stat. 908, but the original section 11 remedy-rescission of the sale-also assumes continuation of the securities.

The background of the 1933 Act is familiar history. During the stock market boom that preceded the Great Depression, a wave of speculation drove up the largely unregulated market in securities. When the market collapsed in 1929, "[f]ully half ... of the securities floated during this period ... proved to be worthless. These cold figures spell[ed] tragedy in the lives of thousands of individuals who invested their life savings, accumulated after years of effort, in those worthless securities." H.R.Rep. No. 85, 73rd Cong., 1st Sess. 2 (1933). The most notorious example was Samuel Insull's sale of several million shares of utility stock to the public. The stock, sold to family members and friends of Insull at $12 or less, opened at $30 in the market and climbed to $149 a share, before it collapsed-to the detriment of a million stock and bondholders. Joel Seligman, *The Transformation of Wall Street* 21-23 (1982).

One of the "foremost" causes of such losses was, in the view of Congress, "the failure to furnish essential information to prospective investors when they were invited to buy securities." I Louis Loss & Joel Seligman, *Securities Regulation* 25 (3d ed. 1989). The broad purpose of the 1933 Act was to require full disclosure to investors, and section 11 was "designed to assure compliance with the disclosure provisions of the Act by imposing a stringent standard of liability on the parties who play a direct role in a registered offering." *Herman & Maclean* v. *Huddleston*, 459 U.S. 375, 381-82, 103 S.Ct. 683, 687, 74 L.Ed.2d 548 (1983). Contemporaneous writings confirm that the main target of section 11 was the sale of registered securities to the public. See 77 Cong. Rec. 2918 (1933) (Rep. Rayburn); Douglas & Bates, *The Federal Securities Act of 1933,* 43 Yale L.J. 171, 174-77 (1933).

Needless to say, there is little resemblance between this scene of ill-informed small investors buying investment

securities on original issue or later through the market and the triangular "forward merger" by which Contel acquired NDS, doubtless after careful study of information that went far beyond the registration statement issued some years before incident to a public NDS offering. This mismatch ought not deprive Contel of a section 11 remedy in any case where section 11's "acquiring such security" language fits the transaction (for example, a tender offer acquisition by Contel of the NDS shares). The mismatch does, however, create doubt that stretching the language to fit Contel's circumstances can be justified as serving Congress' purpose.

As the Supreme Court has reminded us, the federal securities laws were not designed to provide "a broad federal remedy for all fraud," *Marine Bank* v. *Weaver*, 455 U.S. 551, 556, 102 S.Ct. 1220, 1223, 71 L.Ed.2d 409 (1982), let alone for all negligence. If Coopers & Lybrand has been careless in certifying the registration statement and Contel relied on that statement in setting the terms of the merger, then state law might or might not provide a remedy, depending on how the state court approached issues of negligence, foreseeability, and standing. Section 11, by contrast, is remarkably stringent where it applies, readily imposing liability on ancillary parties to the registration statement (like accountants) for the benefit even of purchasers after the original offering. Its very stringency suggests that, whatever the usual rule about construing remedial securities legislation broadly *(e.g., SEC* v. *Capital Gains Research Bureau, Inc.*, 375 U.S. 180, 195, 84 S.Ct. 275, 284, 11 L.Ed.2d 237 (1963)), some care should be taken before section 11 is extended beyond its normal reading.

This is apparently a case of first impression, and virtually none of the precedents provides much assistance. Versyss' best case is *SEC* v. *National Securities*, 393 U.S. 453, 466,

89 S.Ct. 564, 571, 21 L.Ed.2d 668 (1969), which it offers for the proposition that the transfer of stock in a merger is a purchase or sale of securities under section 10(b) of the 1934 Act, 15 U.S.C. § 78j(b). It is surely true under *National Securities* that the NDS stockholders would be treated for purposes of section 10(b) as having "sold" their NDS stock and "purchased" Contel stock in return. Nothing in *National Securities* suggests, however, that Contel is to be treated as "acquir[ing]" the NDS securities. The key to the anomaly-that a sale of securities may occur without a purchaser of securities-is that the securities, although relinquished by the seller are never acquired by anyone because they cease to exist as securities (by operation of merger law) at the same time as they are relinquished.[4/]

The lack of precedent for applying section 11 to our facts may mean only that the acquiring company in a merger transaction rarely relies upon statements in an earlier registration statement of the acquired corporation. On the other hand, it may be that such reliance has occurred from time to time but, when the registration statement proved false and the reliance misplaced, no one thought that section 11 applied. Even so, applying section 11 to merger acquisitions might not unfairly upset settled expectations; under section 11, accountants are held to demanding standards when they certify registration statements and are liable to remote

---

[4/] The same reasoning disposes of *Junker* v. *Crory*, 650 F.2d 1349 (5th Cir. 1981), in which the court held that a merger may involve a purchase or sale of securities under section 12(2) of the 1933 Act, 15 U.S.C. § 77l(2) § 77(2) (condemning material misstatements or omissions in connection with such a transaction). The court there was concerned with whether the plaintiff who surrendered securities in the merged corporation and received new securities in the surviving corporation was a purchaser or seller (the court said the plaintiff was both). Once again, this case would treat the NDS stockholders as possible plaintiffs but says nothing about the status of Contel.

purchasers well beyond more predictable common law limits. But section 11 does not make accountants liable to everyone for any harm remotely flowing from a false or inaccurate statement. *See Abbey* v. *Computer Memories, Inc.*, 634 F. Supp. 870, 875 (N.D. Cal. 1986). The problem, simply put, is to determine where Congress drew the line.

Many statutes, notably statutes of limitation, set limits that create arbitrary stopping-points for liability. Here, it has been assumed that Contel might well have a claim under section 11 if it had acquired the NDS stock in a tender offer and later merged it out of existence. It is even more clear that it would have no claim whatever if the Contel-NDS transaction had been framed as a pure acquisition of NDS *assets*. Faced with a merger transaction that fits neatly into neither category, any construction of the statute will leave discontinuities and a sense of lingering unease. For us, there is a greater conformity to language and less unease in concluding that a defunct security in a non-existent corporation is not a "security" with the meaning of section 11.

The judgment of the district court is *affirmed.*

TORRUELLA, Circuit Judge (dissenting).

Section 11 of the Securities Act of 1933, 15 U.S.C. § 77k(a), provides that "any person *acquiring* [a] security" whose registration statement "contained an untrue statement of material fact or omitted to state a material fact required to be stated may sue "every accountant ... who has with his consent been named as having prepared or certified any part of the registration statement" (emphasis added). This section should impose liability on Coopers & Lybrand in this case.

I arrive at my conclusion by reading the plain language of § 11 and deferring to the ordinary and common meaning of its words. *See Aaron* v. *SEC*, 446 U.S. 680, 685, 100 S.Ct. 1945, 1950, 64 L. Ed. 2d 611 (1980) (construing § 17 of Securities Act of 1933 in light of plain meaning). In its plain meaning, "acquire" means "to come into possession, control, or power of disposal of often by some uncertain or unspecified means." *Webster's Third New International Dictionary* 18 (1981); *see also Black's Law Dictionary* 41 (4th ed. 1951) (defining "acquire" similarly). "Security" is defined by the statute, Securities Act of 1933, § 2(1), 15 U.S.C. § 77b(1) and the NDS stock, prior to the merger, was covered by this definition.

The issue in this case, as I see it, is whether Versyss ever gained possession, control or power of disposal over NDS stock. In this regard, section 2.2 of the Agreement and Plan of Reorganization, setting forth the terms of the merger, plainly states that "each share of NDS Stock ... by virtue of the Merger and without any action on the part of the holder thereof, [shall] *be converted into and exchanged for*" Contel Stock (emphasis added).

The words "be converted into and exchanged for" indicate an acquisition of NDS stock by Contel in that Contel gained possession, control, or power of disposal pursuant to the merger. That is, by virtue of the merger, Contel sold Contel securities which were issued in the merger to stockholders of NDS, and bought all shares owned by NDS stockholders. That the NDS stock ceased to exist following the consummation of the merger is of no consequence because Contel acquired the stock prior to such extinction. Indeed, Contel gained its ability to extinguish NDS stock as a result of its acquisition.

Moreover, § 11, like all securities statutes, must be construed "flexibly to effectuate its remedial purpose." *SEC* v. *Capital Gains Research Bureau*, 375 U.S. 180, 195, 84 S.Ct. 275, 285, 11 L.Ed.2d 237 (1963); *see also Affiliated Ute Citizens of Utah* v. *United States*, 406 U.S. 128, 151, 92 S.Ct. 1456, 1471, 31 L.Ed.2d 741 (1972). In this regard, the Supreme Court has found that Congress passed § 11 to "assure compliance with the disclosure provisions of the Act by imposing a stringent standard of liability on the parties who play a direct role in a registered offering." *Herman & MacLean* v. *Huddleston*, 459 U.S. 375, 381-82, 103 S.Ct. 683, 687, 74 L.Ed.2d 548 (1983) (citations omitted). Thus, Congress imposed essentially fiduciary standards upon those who sign registration statements, including ethical and competence standards meant to ensure sound and honest business practices. H.R.Rep. No. 152, 73d Cong., 1st Sess. 23 (1933). Accountants such as Coopers & Lybrand have a particularly heavy responsibility to the public. H.R.Rep. No. 85, 73d Cong., 1st Sess. 9 (1933).

Interpreting "acquire" to include mergers consummated by stock exchange, such as the one which occurred here, furthers these goals. In passing § 11 Congress wished to control unsound and fraudulent business practices. Whether an acquisition occurs pursuant to a simple sale or a complex merger, the threat of such practices exists, and § 11 should protect all innocent purchasers against them.

The holding of the majority, on the contrary, precludes the application of § 11 to any merger like the one presented here, and thus allows parties to structure their transactions in the form of such a merger to circumvent the application of § 11. Such an end-run around § 11 hardly effectuates its broad remedial purpose.

As such, I dissent.

Appendix B.

UNITED STATES COURT OF APPEALS
FOR THE FIRST CIRCUIT

No. 92-1212

VERSYSS INCORPORATED,
Plaintiff, Appellant,

v.

COOPER AND LYBRAND, ETC., ET AL.,
Defendants, Appellees.

BEFORE

Torruella, Cyr and Boudin, Circuit Judges

ORDER OF COURT

Entered: January 21, 1993

Upon consideration of appellant's petition for rehearing,

It is ordered that the Petition for rehearing be denied

By the Court
Clerk

Appendix C.

UNITED STATES DISTRICT COURT
DISTRICT OF MASSACHUSETTS

----------x
VERSYSS INCORPORATED,
Plaintiff

v. Civil Action
No. 88-121-K

COOPERS & LYBRAND,
A Partnership, and
WILLIAM K. O'BRIEN,
As Managing Partner of
Coopers & Lybrand,
Defendants
----------x

Memorandum and Order
January 15, 1992

Before:

HON. ROBERT KEETON, District Judge

JUDGE KEETON: This is a federal securities action under Section 11 of the Securities Act of 1933, 15 U.S.C. § 77k. Plaintiff has also alleged state law negligent misrepresentation claims. On May 17, 1985, Continental Telecom, Inc. ("Contel") and its subsidiary, NDS Merger Corporation ("Contel Subsidiary"), entered into an Agreement and Plan of Reorganization (attached as Ex. 1 of

Aff. of Henry A. Sullivan (Docket No. 177)) ("Merger Agreement") with the principals of Northern Data Systems, Inc. ("NDS") whereby it was agreed that NDS would be merged into Contel Subsidiary. At that time, NDS was a corporation with publicly traded stock that had been issued in a public offering pursuant to a prospectus and registration statement allegedly negligently audited by defendant Coopers & Lybrand. The Merger Agreement was approved by the shareholders of NDS on July 16, 1985. This lawsuit was initiated by Contel in January 1988, and Versyss Inc. was substituted as plaintiff upon assignment by Contel of its rights in this litigation to Versyss. At a hearing conducted on January 2, 1992, the court announced its conclusion that summary judgment must be entered for the defendants on the parties' cross-motions for summary judgment. The parties were given additional time to submit briefs on how best to proceed with respect to plaintiff's pendent state claims. This Memorandum and Order explains the reasons for the court's announced conclusion, and disposes of the remainder of the case.

I.

Defendant contends that neither the plaintiff in this case, nor any of the entities to whose claims plaintiff has allegedly succeeded, is a "person" in the broad legal sense (that is, either a natural person or some other legal entity) for whom section 11 of the 1933 Act, or judicial decisions interpreting and applying that section, creates a remedy.

In addressing this contention, I first state in another and more elaborate and specific way what I understand the argument to be. The defense presented by this motion for summary judgment is that § 11 supports a claim only if it is a claim (i) of a statutorily described type, (ii) made by a plaintiff who is a person or entity within a statutorily

prescribed group, (iii) against a defendant who is a person or entity within a statutorily prescribed group. Thus, the argument goes, precedents as to who may, for example, bring a 10b-5 type claim do not apply here, nor do precedents as to who may be a proper 10b-5 defendant. The matters of (i) defining the elements of a claim, (ii) defining the potential plaintiff group, and (iii) defining the potential defendant group are interrelated.

Is this a valid defense? The parties have not brought to the court's attention any precedent answering precisely this question, and the court has found none. Thus, the issue may be seen as one of first impression. Given the almost six decades since enactment of the 1933 Act, perhaps the absence of precedent to show that at least such a claim has been asserted is itself a basis for inferring that plaintiff's claim is so unusual that the bar has not thought it likely to be worth asserting. It may be said in response, however, that fashions and practices regarding mergers and acquisitions may change with time, and new questions may arise, even after decades of experience. So rather than simply conclude that I should dismiss plaintiff's claim because of the absence of supporting precedent, I proceed to examine the arguments advanced by the parties, and the analyses they suggest in their briefs and oral arguments.

II.

Defendants contend that § 11 requires an acquisition of stock issued pursuant to a prospectus, and that no such acquisition took place in this case. The relevant facts are derived from the language of the Merger Agreement, and are not in dispute. Section 11 provides, in relevant part:

> In case any part of the registration statement, when such part became effective, contained an untrue statement of a material fact or omitted to state a material fact required to be stated therein or necessary to make the statements therein not misleading, any person acquiring such security ... may ... sue ... every accountant ... with respect to the statement in such registration statement, report, or valuation which purports to have been prepared or certified by him ... .

15 U.S.C. § 77k(a) (emphasis added). At the heart of the present dispute is the meaning of the phrase "acquiring such security."

Plaintiff argues that Contel acquired the NDS stock issued pursuant to the prospectus at the time that the Merger Agreement was executed, and, at the latest, by the time the NDS shareholders approved the merger. The merger was not effective until the date that the Secretary of State of Massachusetts issued a certificate of merger. See Merger Agreement § 5. Thus, it is contended that under principles of contract law, Contel had purchased, and therefore acquired, the rights to NDS stock before the effective date (at which time NDS was extinguished as a separate corporate entity).

This argument must fail. First, it commits the very fallacy that counsel for Versyss attributes to defense counsel -- proceeding on a technical and metaphysical basis rather than looking at the substance of the agreement. The answer to any such argument is that the sequence and timing of steps toward effectuating the agreement are less important than the substance of the agreement as a whole.

Owners of the stock issued pursuant to the NDS prospectus possessed certain rights that coincide with stock ownership. Among those rights were the rights to receive dividends, if such were ever issued, and the right to vote in corporate elections. These rights were never acquired by Contel. The Merger Agreement provided that NDS stock would automatically be converted into and exchanged for Contel stock upon completion of the merger. Merger Agreement § 2.2. Thus, NDS shareholders obtained Contel stock in exchange for NDS stock as one of the steps in the effectuation of a single agreement for a merger that destroyed the corporate existence of NDS. Even if it may be said that from Contel's perspective, Contel acquired possession of the substance of NDS, it is also true that as part of the same Merger Agreement the characteristics and the value of the NDS shares as they existed before the Merger Agreement was entered into were extinguished. No right to dividends or to vote NDS shares was ever passed on to Contel by virtue of its acquisition of the NDS shares, as plaintiff's counsel correctly admitted at argument. Contel did acquire somewhat different rights that may have had as much practical value, but it did not do so by "acquiring such securities." Regardless of what one chooses to mark as the time when Contel received either the shares of stock or the right to receive them, what it received came pursuant to the Merger Agreement and subject to all its terms and conditions. Contel never received or had a right to receive securities having the same characteristics as those issued pursuant to the allegedly erroneous prospectus and registration statement.

Plaintiff contends that it is improper to focus on the moment of merger. If one looks to the moment of "closing," plaintiff argues, it is apparent that NDS continued to exist. If one takes that view, however, it also follows that at the moment of closing, Contel had not yet acquired NDS shares

of stock. Instead, Contel then had only the right to acquire NDS shares at a later date. Plaintiff asserts that a distinction between acquiring stock and acquiring the right to acquire stock at a later time is a distinction without a difference under contract law principles. In fact, however, the more substantive point that plaintiff's whole argument misses is exposed when basic contract principles are applied to the Merger Agreement.

Contel's rights, at each point in time through the steps of the merger, must be determined by reading the whole Merger Agreement. Under that agreement, Contel never at any time acquired the right to dividends on NDS stock or the right to vote that stock, nor did it ever acquire the right to acquire such rights. Contel could not have acquired the NDS shares unencumbered -- Contel's right to own the shares was derived from the same Merger Agreement that called for the termination of NDS' corporate existence. Plaintiff stated several times at oral argument that this fact was a mere result of Contel's agreement, and that a different agreement could have been reached if Contel had so wanted. This assumption is unwarranted, however, because this was a mutual agreement. Neither party to the agreement, and no successor, can now validly claim that either one or the other of the parties alone could have chosen to make the agreement different. Moreover, having chosen to agree to structure the merger as it did, Contel cannot now complain successfully that if things were different it could have been a § 11 plaintiff. Versyss, standing in Contel's shoes, is in no better position.

III.

Plaintiff's remaining contentions may be disposed of summarily. Plaintiff contends that § 11 evinces a strong

Congressional policy preference for holding experts such as Coopers & Lybrand liable for their errors. For example, § 11 places a burden of proof on defendants rather than on plaintiffs on the issue of diligence. Plaintiff maintains that the phrase "acquiring such security" ought to be construed broadly rather than narrowly in keeping with the purpose of § 11 to hold experts liable. However, § 11 is designed to facilitate suits for compensation against experts by persons who rely on expert analyses. The class of persons who may bring § 11 suits is therefore narrow -- those persons who acquire the certified securities. Plaintiff does not fall into that class. Recognition of this point also disposes of plaintiff's arguments based upon other sections of federal securities law. Although § 11 establishes a high standard of liability for certain defendants, the availability of a § 11 remedy is limited to a narrow class of plaintiffs. Case law interpreting similar phrases in other statutory provisions cannot be imported readily to explain the meaning of the phrase "acquiring such security" as used in § 11.

Finally, plaintiff contends that the rule here announced exalts form over substance. In the present case, a so-called "reverse merger" was executed in which NDS was merged into Contel Subsidiary, and Contel Subsidiary was the surviving corporation. If a "forward merger" had been accomplished, NDS would have been the surviving entity, and NDS shares would have retained their characteristics. Indeed, it is argued that NDS shares could have been acquired by Contel through a tender offer. Even if it be assumed that in either of the latter cases, Contel would have acquired "such" NDS shares within the meaning of § 11, plaintiff's contention is answered simply. Section 11 is concerned only with the acquisition of securities in the circumstances it defines, not with all other possible forms of acquisitions of corporate interests. After all, § 11 is a section of a securities act. Plaintiff's claim in this case that

it was harmed in its acquisition of NDS itself is not affected by my ruling here. Thus, plaintiff may be correct that a substantive tort claim ought not to depend upon the form of acquisition of NDS. That issue is not now before this court. Instead, plaintiff's claim here is that it was harmed in its acquisition of NDS securities that were the subject of the Coopers & Lybrand certification. That claim cannot succeed.

IV.

The court assumed jurisdiction over plaintiff's state claims pendent to its jurisdiction over the § 11 claim. Having resolved the § 11 claim, I must now consider whether to dismiss the pendent state claims. See *United Mine Workers* v. *Gibbs*, 383 U.S. 715 (1966). The parties were invited to file briefs before the court on this issue, and an extension of the time to do so, to and including January 9, 1992, was granted by the court. Nothing further has been submitted.

Because all of the claims remaining in the case are currently pending in parallel litigation in state court, and because all remaining contested issues of law are more appropriately resolved in state court, I conclude that the remaining claims in this action should be dismissed without prejudice.

ORDER

For the foregoing reasons, it is hereby ORDERED:

(1) Defendants' motion for summary judgment is ALLOWED.

(2) Plaintiff's cross-motion for partial summary judgment is DENIED.

(3) All other claims in this action are dismissed without prejudice.

Final judgment in accordance herewith will be issued forthwith.

_____

United States District Judge

UNITED STATES DISTRICT COURT
DISTRICT OF MASSACHUSETTS

----------x
VERSYSS INCORPORATED,
Plaintiff

v.

Civil Action
No. 88-121-K

COOPERS & LYBRAND,
A Partnership, and
WILLIAM K. O'BRIEN,
As Managing Partner of
Coopers & Lybrand,
Defendants
----------x

Final Judgment
January 15, 1992

Before:

HON. ROBERT KEETON, District Judge

For the reasons stated in the Memorandum and Order of this date, it is hereby ORDERED:

(1) Count I of plaintiff's Third Amended Complaint is dismissed with prejudice.

(2) All other claims in this case by any party are dismissed without prejudice.

Costs are awarded to defendants in this action.

United States District Judge

Appendix D.

15 U.S.C. § 77k(a)

(a) Persons possessing cause of action; persons liable. In case any part of the registration statement, when such part became effective, contained an untrue statement of a material fact or omitted to state a material fact required to be stated therein or necessary to make the statements therein not misleading, any person acquiring such security (unless it is proved that at the time of such acquisition he knew of such untruth or omission) may, either at law or in equity, in any court of competent jurisdiction, sue—

(1) every person who signed the registration statement;

(2) every person who was a director (or person performing similar functions) or partner in, the issuer at the time of the filing of the part of the registration statement with respect to which his liability is asserted;

(3) every person who, with his consent, is named in the registration statement as being or about to become a director, person performing similar functions, or partner;

(4) every accountant, engineer, or appraiser, or any person whose profession gives authority to a statement made by him, who has with his consent been named as having prepared or certified any part of the registration statement, or as having prepared or certified any report or valuation which is used in connection with the registration statement, with respect to the statement, in such registration statement, report, or valuation, which purports to have been prepared or certified by him;

(5) every underwriter with respect to such security.

If such person acquired the security after the issuer has made generally available to its security holders an earning statement covering a period of at least twelve months beginning after the effective date of the registration statement, then the right of recovery under this subsection shall be conditioned on proof that such person acquired the security relying upon such untrue statement in the registration statement or relying upon the registration statement and now knowing of such omission, but such reliance may be established without proof of the reading of the registration statement by such person.

15 U.S.C. § 77k(b)

(b) Notwithstanding the provisions of subsection (a) no person, other than the issuer, shall be liable as provided therein who shall sustain the burden of proof -

(1) that before the effective date of the part of the registration statement with respect to which his liability is asserted (A) he had resigned from or had taken such steps as are permitted by law to resign from, or ceased or refused to act in, every office, capacity, or relationship in which he was described in the registration statement as acting or agreeing to act, and (B) he had advised the Commission and the issuer in writing that he had taken such action and that he would not be responsible for such part of the registration statement; or

(2) that if such part of the registration statement became effective without his knowledge, upon becoming aware of such fact he forthwith acted and advised the Commission, in accordance with paragraph

(1), and, in addition, gave reasonable public notice that such part of the registration statement had become effective without his knowledge; or

(3) that (A) as regards any part of the registration statement not purporting to be made on the authority of an expert, and not purporting to be a copy of or extract from a report or valuation of an expert and not purporting to be made on the authority of a public official document or statement, he had, after reasonable investigation, reasonable ground to believe and did believe, at the time such part of the registration statement became effective, that the statements therein were true and that there as no omission to state a material fact required to be stated therein or necessary to make the statements therein not misleading; and (B) as regards any part of the registration statement purporting to be made upon his authority as an expert or purporting to be a copy of or extra act from a report or valuation of himself as an expert, (i) he had, after reasonable investigation, reasonable ground to believe and did believe, at the time such part of the registration statement became effective, that the statements therein were true and that there was no omission to state a material fact required to be stated therein or necessary to make the statements therein not misleading, or (ii) such part of the registration statement did not fairly represent his statement as an expert or was not a fair copy of or extract from his report or valuation as an expert; and (C) as regards any part of the registration statement purporting to be made on the authority of an expert (other than himself) or purporting to be a copy of or extract from a report or valuation of an expert (other than himself), he had no reasonable ground to believe and did not believe, at the time such part of the registration statement became effective, that the statements therein were untrue or that there was an

omission to state a material fact required to be stated therein or necessary to make the statements therein not misleading, or that such part of the registration statement did not fairly represent the statement of the expert or was not a fair copy of o r extract from the report or valuation of the expert; and (D) as regards any part of the registration statement purporting to be a statement made by an official person or purporting to be a copy of or extract from a public official document, he had no reasonable ground to believe and did not believe, at the time such part of the registration statement became effective, that the statements therein were untrue, or that there was an omission to state a material fact required to be stated therein or necessary to make the statements therein not misleading, or that such part of the registration statement did not fairly represent the statement made by the official person or was not a fair copy of or extract from the public official document.

15 U.S.C. § 77k(e)

(e) Measure of damages; undertaking for payment of costs. The suit authorized under subsection (a) may be to recover such damages as shall represent the difference between the amount paid for the security (not exceeding the price at which the security was offered to the public) and (1) the value thereof as of the time such suit was brought, or (2) the price at which such security shall have been disposed of in the market before suit, or (3) the price at which such security shall have been disposed of after suit but before judgment if such damages shall be less than the damages representing the difference between the amount paid for the security (not exceeding the price at which the security was offered to the public) and the value thereof as of the time such suit was brought: Provided, That if the defendant proves that any portion of all of such damages represents

other than the depreciation in value of such security resulting from such part of the registration statement, with respect to which his liability is asserted, not being true or omitting to state a material fact required to be stated therein or necessary to make the statements therein not misleading, such portion of or all such damages shall not be recoverable. In no event shall any underwriter (unless such underwriter shall have knowingly received from the issuer for acting as an underwriter some benefit, directly or indirectly, in which all other underwriters similarly situated did not share in proportion to their respective interests in the underwriting) be liable in any suit or as a consequence of suits authorized under subsection (a) for damages in excess of the total price at which the securities underwritten by him and distributed to the public were offered to the public. In any suit under this or any other section of this title [15 USCS §§ 77a et seq.] the court may, in its discretion, require an undertaking for the payment of the costs of such suit, including reasonable attorney's fees, and if judgment shall be rendered against a party litigant, upon the motion of the other party litigant, such costs may be assessed in favor of such party litigant (whether or not such undertaking has been required) if the court believes the suit or the defense to have been without merit, in an amount sufficient to reimburse him for the reasonable expenses incurred by him, in connection with such suit, such costs to be taxed in the manner usually provided for taxing of costs in the court in which the suit was heard.

[This page is intentionally left blank.]